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July 1992 (First Of Two July Issues)

INDECISION IN STATE FINANCES

Few Decisions At Decision Time

"Budgeting has become a year-around process." -- This is a common complaint in many states from legislators tired of prolonged regular legislative sessions. It is also a complaint of budget staffs reminiscing about days when the budget decision crunch came shortly before the beginning of the new fiscal year, followed by months of relative calm.

It is hard to measure whether more and more budget decisions have been shifted away from normal schedules for making them. Certainly, this has been true in **Texas**, where court decisions on school finance have kept the state's major spending category in a state of constant flux. It was true in FY 1992, when revenue shortfalls required most states to revisit their budgets for administrative cuts, special legislative actions, or both. But it may not prove to be a permanent change in state budget procedures, as distinct from a response to the special circumstance of shortfalls occurring after budgets have been set.

Another factor, elections, is at work in 1992. The budget decisions so far this year have been characterized by an extraordinary resistance to make decisions that would balance state budgets over the long term. That is, a reluctance to raise taxes and a reluctance to make major cuts in spending patterns. Instead, in most states, the choices have been deferrals of spending, acceleration of revenues, and simply finding ways to ignore imbalance until after elections.

In some states, the result has been an inability to reach any decisions quickly when confronted by major unacceptable alternatives. The best examples are **California** and **Florida**. In others, such as **Texas**, major decisions like revising the method of financing schools are being held until after elections. In yet others, the delay in decisionmaking isn't obvious. Instead, the decisions made in states like **New York** appear final, but may not hold up for the entire fiscal year. As a result, this year at least, many important state fiscal decisions will be made during the fiscal year. There will probably be some special sessions on finances in December and many states will make major budget revisions early next year. There will likely be some tax increases involved.

One example will probably be **Ohio**. The governor urged "sin tax" increases which the speaker rejected as being targeted at the poor. The governor rejected the speaker's plan to target the rich with income tax increases on those earning $200,000 or more calling it "a smoke screen." The result is no tax increase to finance FY 1993 spending. But the speaker commented in late June:

I think we should wait until sometime around December or January. We should look at the whole tax structure. I never have, and would not, run from my responsibilities to have a balanced budget.

Budget Cutting In New Jersey

New Jersey, which held its legislative elections in 1991, is not on the same election cycle as other states. Its new veto-proof Republican majority hasn't so far shown the reluctance to make major fiscal decisions that has appeared in many other states. The majority repealed the one-cent sales tax increase that was part of the unpopular tax package of 1990 and turned attention to balancing the new budget.

That budget was hard to balance with the tax cut because the Garden State was one of the states most seriously affected by the recession. To propose a budget of $15.7 billion, the governor used many of the devices for balancing budgets without either raising taxes or cutting spending, including major revisions in retirement contributions.

The Republican's plan trimmed the total to $14.6 billion. The impacts were disputed. Sponsors predicted it would produce 1,500-2,000 layoffs in addition to the loss of about 2,500 jobs from attrition contemplated in the governor's budget. Florio Administration officials predicted even greater job losses from the plan. The Department of Human Services would lose about $190 million of the $3.7 billion budget request, with cuts concentrated in general assistance. The largest cut, $385 million, was in the $685 million homestead rebate program. The state transit agency would lose $35 million.

The treasurer said the plan was $226 million out of balance. Republican leaders replied if the governor really believed that, it was his duty to use vetoes to bring it into balance. Democrats and interest groups, frustrated by lack of hearings on the cuts, held a rump committee session to publicize cuts in higher education, general assistance, and state operating programs. Department heads warned of closed state parks, uncleared snow on highways, and loss of federal matching money. The debate as the budget passed the Senate on a party-line vote was spirited. An opponent lamented, "I don sackcloth and cover myself with ashes and tearfully cast my vote against this budget." A proponent hoped it was "only the beginning of tax cuts" and that there would be more cuts next year.

Avoiding Tough Decisions, Mental Health

Despite talk of layoffs and shrinking payrolls that constantly gains headlines in many states, there have been few savings in the labor-intensive operations of state residential institutions for prisoners and mental health patients. The barriers to corrections savings are rising prisoner counts and state officials often willing to pay the costs to back stiff sentencing and avoid crimes by prisoners in alternative corrections programs.

These explanations don't apply to mental health. The situation in **Ohio** is indicative of that in most states. Advances in pharmacology and changes in treatment doctrines have cut admissions to state facilities from a peak of 22,000 in 1971 to 11,800 in 1990. During the same period, the resident population dropped from 28,500 to 3,100. But the reduction hasn't been fully reflected in institutional closings. Instead, Ohio is operating five hospitals at 40% or less of capacity and one at 18%. Not surprisingly the ratio of staff to patients has grown in the past 20 years from 0.5 staff to one patient to 1.8 staff per patient.

State officials have shied away from the obvious alternative of institutional closings for reasons similar to Congressional reluctance to close defense installations. The facilities are often the major employers in otherwise depressed areas. A high percentage of workers could not find other employment locally. Institutional closings or scale-backs such as closing hospital wings have been pushed by some governors (e.g., in **Massachusetts** and **Virginia**) but have often become mired in controversy.

Privatization, More Talk Than Action

Many **Reports** readers and speech audiences, particularly business groups, are consistently interested in the extent to which state fiscal problems are causing moves to "privatize" the provision of state services. At least this year, the answer appears to be little, if any, depending on how "privatization" is defined. While the issue generates massive quantities of books and studies (see Technical Notes), the pace of policy change is slow.

The most obvious areas for privatization of state services are those where: (1) private provision of the services is common in the American economy and (2) some states already use the private sector. This view was taken by the business-oriented group in New Jersey (see related article) which declined to include privatization savings in its cost-cutting recommendations. Instead, it commented, "Priority consideration for potential privatization should be given ... to activities now conducted directly by the state government for which there are currently private markets, such as the provision of security guards, printing, payroll recordkeeping and paycheck issuance, and groundskeeping."

If privatization ever became a major influence in state policy, two activities would signal the change. Private firms have proven track records in liquor sales and insurance. Yet about a third of the states sell liquor and about a fourth are in the insurance business, primarily in Workers' Compensation. While there is some discussion of change for these functions, there has been little movement of them to (or from) the private sector in decades.

The major budget-motivated moves for privatization aren't closely related to the philosophical debates about the relative competence and costs of public and private sector enterprises.

To raise cash or to shift capital outlays outside the budget, some states are selling assets in sale-leaseback arrangements or replacing a policy of purchasing buildings and equipment with leasing. In order to maximize Medicaid reimbursement and follow current treatment doctrines, many states are shifting patients out of state-provided public health and mental health settings into settings where they are served by private providers, such as private psychiatric hospitals and community mental health agencies.

The truly big-ticket areas of potential privatization are being debated and, to some extent, demonstrated, but with little immediate relation to current state fiscal problems. Examples are: (1) choice in elementary and secondary education, (2) use of scholarships and other student subsidies rather than subsidizing institutions in higher education, (3) private turnpikes and bridges, and (4) contracting for spaces in correctional institutions.

ASSESSING BALANCED BUDGET REQUIREMENTS

Passing The Budget-Balancing Buck

In the many states with divided party control of the governor's office and the legislature, this year is seeing examples of attempts to make the other party's elected officials the bearers of bad news. In **Michigan**, the governor (R) sought to devise ways to rebalance the FY 1992 budget by informal consultations with legislative leaders (divided control). Democratic legislators reminded the governor that under Michigan law the governor is obligated to make findings that fiscal problems exist and take action to deal with them. The governor discharged this responsibility, but not until pointing out that the criticism last year was for acting without consultations Democrats thought were necessary.

In many states, as in Michigan, the governor has both a duty and the power to take administrative steps to cure shortfalls in the current fiscal year. But both the law and the politics become confusing when there are potential conflicts between appropriations, which the governor may restrict in these states, and substantive legislation. This has been the major issue in debates on the FY 1993 budget in **California**. Both houses have passed bills which give the governor considerable responsibility to decide cuts, but don't allow him to control laws that govern spending, such as those setting welfare payment levels. The governor argues this approach is unacceptable. His approach, scheduled to be put before voters by initiative petition, would give him more unilateral power than legislative leaders find acceptable to revise substantive legislation in the name of budget cutting.

Gubernatorial Leadership And Executive Budget Concepts

What happens when the problem of balance arises for the following year? The governor clearly has no power, as the legislature has the power to set both appropriations and tax levels. The governor's obligation to recommend a balanced budget has already been discharged. When, given more current information about revenues and spending, everyone concedes that the budget doesn't balance, must the governor revise the executive budget recommendations? The situation is not contemplated in state constitutions and generally not covered by state budgeting statutes, so the governor isn't required to make formal amendments to the spending and tax recommendations. But when governors don't act in these situations, they violate the concept of the executive budget.

The executive budget makes sense on two bases. The first is that chief executives are needed to provide leadership and a sense of direction. The second, more mundane one, is that an executive agency is needed to keep budget concepts (e.g., handling price and pay assumptions) consistent and to formulate and implement the details of a budget, as well as to staff the chief executive's leadership role. Using this concept, some governors make adjustments in their recommendations throughout the legislative process. By doing this, they always maintain the posture that their recommendations are what they, under present circumstances, believe to be best for the state and consistent with balanced budget requirements. Sometimes the changes to the original budget are formal amendments to the budget recommendations. Usually, they aren't.

All this works reasonably smoothly in some situations, but not others. Though few in the Empire State would agree, **New York** is a consistent example of such a smooth process. **California** sometimes is and sometimes isn't. This year, it isn't. In California, the governor concedes that the estimates underlying his budget are overly optimistic. The obvious conclusion is that (short of incredible degrees of gimmickry) California must either raise taxes or not honor the constitutional requirement for automatic growth in spending for elementary and secondary education and community colleges. No one wants to be the first to say this, or to pick a solution to advocate. So in California, as in Michigan, governors and legislators each waited for the other to make the first move.

It is not necessary to have an executive budget at all. The legislature can collect budget recommendations from state departments and interest groups, develop its own starting point for consideration, and move to enactment with no input from chief executives. The Congress operated this way until 1921. Many states -- most notably **Mississippi**, **South Carolina**, and **Texas** -- have functioned this way with variants such as gubernatorial participation on a budget board or an executive budget which isn't necessarily the starting point for legislative deliberation. Some states with strong executive budget principles in their laws use a legislative system in practice, with **Colorado** a long-standing example.

Other states have different laws and traditions. For example, in **Minnesota** and **Wisconsin**, legislators act bound by balanced budget requirements. They usually send more or less balanced packages, taxes and all, to governors even if anticipating that some of the spending will be vetoed. In one-party states, particularly in the South, the state's leadership frequently operates by consensus and the only rigid formal positions are the ones in enacted legislation. **Georgia**'s handling of its fiscal adjustments is a good example.

Another variation of the controversies over executive and legislative roles appeared this year in **New Jersey** and **Ohio**. The governors submitted budgets they contended were balanced. Their legislature made tax decisions eliminating some revenues assumed in the budget. In New Jersey, they repealed a cent of the sales tax. In Ohio, they rejected the governor's proposed increases in taxes on alcoholic beverages and tobacco. Both governors concluded that the resulting budget was out of balance.

The parallel ended when Ohio's governor announced a series of major administrative reductions in spending which he said were necessitated by the legislative rejection of his tax plan. Legislative leaders of both parties suggested the cuts were too early, too harsh, or both. New Jersey's governor didn't act as quickly. Garden State legislative leaders are saying that if the governor thinks the budget doesn't balance, it is his responsibility to use his veto and administrative powers to reduce spending. The governor's temptation was to blame an impossible situation on the legislature.

Balanced Budget Requirements In Theory

Responding to situations like these and to federal interest in state balanced budget requirements as precedent for a national balanced budget amendment, the National Association of State Budget Officers recently completed a survey of exactly how the state requirements work. The report notes that state laws may require a balanced budget at one or more of three stages: (1) when submitted by governors, (2) when enacted by legislatures, or (3) when the fiscal year ends. Individual state provisions "may not specify any of the three conditions but, instead, might simply say that the governor must ensure that there are sufficient revenues to cover expenditures contained in the budget." The report concludes that balanced budget tradition, "rather than enforcement provisions or the threat of lower bond ratings, is the most important factor contributing to balanced state budgets."

The survey of state executive budget agencies concludes that 36 governors have the power to implement budget cuts without legislative approval if necessary to maintain budget balance. Many states restrict this power by specifying that cuts must be equal in each program or that they cannot exceed a maximum amount. Except in **Indiana** and **North Carolina** where NASBO says governors have no budget veto power, governors can seek to restore budget balance by vetoes of appropriations bills and, in many states, by vetoing and/or adjusting individual line items and substantive legislation passed with the budget.

Authority to balance budgets by increasing taxes is reserved to the legislature in all states. Nine states constitutions (**Arkansas**, **California**, **Delaware**, **Kentucky**, **Louisiana**, **Mississippi**, **Ohio**, **Oklahoma**, and **South Dakota**) require more than a simple majority to pass revenue increases.

PROSPECTING FOR BUDGET CUTS

The quest for savings is primarily the responsibility of state officials, but it can include other players such as business-sponsored permanent organizations and ad hoc management improvement efforts. Recent examples come from three states.

Maine: The Special Commission on Governmental Restructuring viewed Maine's problem as part of a general over-reaching by states in the 1980s:

> *The 1980s has been called the "golden age of the states," a decade in which state revenues grew and state government became a major force in setting the domestic policy agenda in this country. In areas as widely different as welfare and education reform, as public housing and environmental protection, state government filled the policy vacuum left by a federal government strapped with mounting budget deficits.*
>
> *As quickly as states have emerged as leading players in domestic policy, they have found themselves confronting desperate financial situations. As the '80s were a decade of plenty, the 90s promise to be a decade of scarcity.*

The group concluded: "As plenty permitted the states to innovate, experiment, and extend the domestic policy agenda, so scarcity will force the states to focus on management and operations." Its recommendations included consensus revenue forecasting, fiscal notes on proposed legislation, development of six-year plans, changes in the format of the budget, and reorganization of selected state agencies. Maine's primary response to fiscal crisis so far has not been those measures but raising taxes and curtailing expensive program initiatives in such fields as health care and property tax relief.

New Jersey: The Public Affairs Research Institute has presented 22 options which it contends would produce $862 million in savings. The group's recommendations centered on issues common to many states: health care, pensions, privatization, and local government aid. Other recommendations concern state staffing and compensation including: (1) ending automatic step increases, (2) eliminating a special supplement to regular compensation for workplace injuries, (3) no longer rewarding employees at retirement for 50% of the value of unused sick leave, and (4) using contingency staffing, such as part time and seasonal workers, more frequently.

The New Jersey report suggests singling out high-paid employees for layoffs -- for example, by requiring that one in six employees making over $70,000 be eliminated in most departments. The legislature has been working with a variant of this plan, as well as the group's recommendation of substantial reduction in homestead rebates.

Concerned about the high costs of short-term borrowing, the group recommended deliberate delays in payments of vendors, local governments, and families entitled to homestead rebates. It called New Jersey a leader in the use of alternatives for incarceration for convicted offenders and urged expanding concepts like house arrest. Noting three recent well-publicized instances in which offenders in alternative correction settings have been charged with crimes, the Council commented, "requiring 100% success in any program including offenders is an unrealistic, unobtainable standard."

Ohio: The Ohio Report is the product of a business task force that produced 1,600 ideas for saving money, about $430 million a year. Many of the recommendations reflect general management principles (e.g., getting feedback from agency "customers," establishing performance measures, and involving employees in decisionmaking). Recommendations include:

Reorganization to a secretary/coordinator model with department heads reporting through a small number of cabinet secretaries as is done in California, Massachusetts, and Virginia,

Total Quality Management, adopting ideas in vogue in the private sector,

Improving Employee Training, **Program Evaluation**, and **Personnel Procedures** -- recommendations found in most business task force reports,

More Aggressively Seeking Federal Funds, including a Washington office staff position for the function and better tracking of federal grant money, and

Expanding General Obligation Debt, but reducing by an equal amount the revenue bonds Ohio issues for university buildings and other activities to avoid taking bond issue constitutional amendments to voters for approval.

Like most business task forces, the Ohio group avoided programmatic recommendations. For example, the Medicaid discussion considers issues like increasing reimbursements from third parties (e.g., Medicaid recipients also eligible for health insurance reimbursements or recoveries from auto liability insurance) and maximizing federal reimbursements, but doesn't consider restricting persons covered or services provided.

RETRENCHMENT NOT SHOWING IN PAYROLLS

Measuring how completely state leaders adjusted to recession is difficult because the relevant statistics on state and local spending have not yet been issued. One proxy is to compare the earnings gains of state and local workers with earnings gains of all workers. For both groups, earnings reflect both: (1) gains/contractions in the number employed and their hours and (2) wage and salary changes. The table shows the percentage gain for each group and the "excess," the differential earnings growths.

Percent Gain In State-Local And Total Earnings, 1990-1991
Showing Spread -- Excess of S/L Gain Over Total Gain

Rank	State	Excess	Total	S/L	Rank	State	Excess	Total	S/L
1	Idaho	8.3%	3.3%	11.6%	27	Florida	3.6%	3.3%	6.9%
2	Nevada	8.2	5.5	13.7		**United States**	**3.4**	**2.7**	**6.1**
3	Maine	7.4	-1.1	6.3	28	Indiana	3.4	2.5	5.9
4	Kentucky	6.2	4.0	10.2	29	Kansas	3.1	2.6	5.7
5	California	6.1	2.0	8.1	30	West Virginia	2.9	2.8	5.7
6	Washington	6.0	6.4	12.4	31	Georgia	2.8	3.2	6.0
7	Alabama	5.9	4.6	10.5	32	Louisiana	2.7	5.3	8.0
8	Vermont	5.6	0.7	6.3	33	Wisconsin	2.7	3.6	6.3
9	Illinois	5.5	2.7	8.2	34	Virginia	2.5	2.3	4.8
10	Iowa	5.3	0.9	6.2	35	Connecticut	2.4	1.2	3.6
11	New Hampshire	5.2	-1.1	4.1	36	Arizona	2.0	3.9	5.9
12	New Jersey	4.9	1.7	6.6	37	Minnesota	2.0	2.9	4.9
13	Delaware	4.7	3.4	8.1	38	Alaska	1.9	4.6	6.5
14	South Carolina	4.6	2.7	7.3	39	Utah	1.5	6.9	8.4
15	North Carolina	4.4	3.1	7.5	40	New Mexico	1.2	6.2	7.4
16	Oregon	4.4	4.4	8.8	41	Texas	0.9	5.5	6.4
17	Maryland	4.3	1.7	6.0	42	Tennessee	0.6	4.0	4.6
18	Pennsylvania	4.3	2.4	6.7	43	Colorado	0.5	6.2	6.7
19	Nebraska	4.2	2.7	6.9	44	New York	0.5	0.6	1.1
20	Hawaii	4.1	6.7	10.8	45	North Dakota	0.2	4.4	4.6
21	Michigan	4.1	1.2	5.3	46	Mississippi	0.1	4.4	4.5
22	Arkansas	3.9	4.9	8.8	47	Massachusetts	0.0	-0.2	-0.2
23	Ohio	3.9	1.8	5.7	48	Montana	-0.1	7.5	7.4
24	South Dakota	3.9	4.5	8.4	49	Wyoming	-0.8	7.4	6.6
25	Missouri	3.8	2.1	5.9	50	Rhode Island	-3.6	-2.3	-5.9
26	Oklahoma	3.8	2.7	6.5					

Nationwide, state and local pay grew by 6.1%, above the 5.2% expected if payroll growth reflected inflation (4.2%) and population growth (1.0%) during 1991. Recession-depressed private earnings growth was only 2.7%. So, state and local earnings growth surpassed total earnings growth by 3.4%, the "excess" for the United States in the table.

There are massive differences among the states in each of the three categories on the table. The differences are most narrow for total earnings. These declined in four states and showed the highest growth in **Utah** with 6.9%. In six states, led by **Nevada** with 13.7% growth, state and local earnings grew by more than 10% in one year. But two states, **Massachusetts** and **Rhode Island**, actually reduced state and local payrolls.

That state and local payroll growth exceeded private sector growth in 1991 isn't surprising. The budgets involved were those of FY 1991 and FY 1992, before the impacts of revisions made in late 1991 and early 1992. The recession caught most state and local governments at a time when their budgets were predicated on normal economic growth. Adjustments lagged revenue shortfalls because of delays in recognizing the problem, planned hedges like rainy day funds, and reluctance to make the tough decisions involved.

In some states, the economy was skidding at the same time state revenues were buoyed by recent tax increases. Those examples -- like **California**, **Illinois**, **New Jersey**, and **Pennsylvania** -- understandably rank high in the "excess" column. Other states with high "excess" enjoyed economies that had been thriving, generating substantial spending increase momentum. Examples are **Idaho**, **Nevada**, and **Washington**.

There were several formulas for keeping the "excess" state and local payroll growth low. One was having rapid growth in the private sector to match rapid growth in the public sector, as occurred in **Colorado**, **Montana**, **New Mexico**, **Texas**, **Utah**, and **Wyoming**. Another was to maintain state and local payroll growth well below the national average as was done in **Connecticut** and **New York**.

The impact of differing responses by state officials and differing interaction of state and local finances appear clearly among New England states, where the recession came earlier than in the rest of the nation. **Rhode Island** made the most decisive adjustment in public payrolls, as the state retrenched sharply to cover both recession-induced revenue loss and heavy outlays caused by failing financial institutions. Its retrenchment quickly and decisively affected universities and local government as well as regular state employees. **Massachusetts** made similar, but less deep, cuts to be among the four states where state payroll adjustments matched or exceeded those of the overall state economy.

Three other New England states show some of the largest "excesses" on the table. **Maine** was the most severe case because its officials, particularly the governor, refused to recognize the seriousness of the state's revenue problem. **Vermont** maintained rapid spending on payrolls by a combination of local taxes and a state tax increase. **New Hampshire** local governments are little affected by state fiscal conditions because there is little state aid to cut. Property tax revenue growth associated with previous real estate price increases helped propel local payrolls upward even when the state's economy was contracting.

LOCAL GOVERNMENT FINANCES AT RISK

Local Aid Cutbacks: The Fiscal Survey Of The States published by the National Association of State Budget Officers this spring included a summary of strategies for eliminating FY 1992 budget gaps. The three most popular, each mentioned by 18 budget offices, were: (1) eliminating programs, (2) reorganizing programs, and (3) reducing local aid. Another table showed that 24 governors proposed local aid changes in their FY 1993 budgets. Most of these were aid cuts adversely affecting local finances. Those helping local fiscal situations were generally costless to states, such as giving local governments more taxing authority and providing relief from state mandates. Local governments in a few states were also affected by state tax increases. **Minnesota** ended exemptions for local government purchases. **New Mexico** began to tax certain local government sales.

In most states, the pattern is to attempt to protect school aid and even increase it while general purpose aid, such as revenue sharing for cities and counties, is cut. In states following this strategy, like **Massachusetts**, where municipalities run schools, this difference in treatment doesn't make much difference. In most states, it means that aid to school districts is increasing while aid to cities and counties is being frozen or cut. The governor's proposals for the **Illinois** budget are an example. Federal aid has also been shifting. More money is flowing to schools and to states for AFDC and Medicaid and less is going to cities and counties.

State Mandates: Unfunded federal mandates remain a major concern of state officials, with constant fear that federal elected officials will deal with their desires to make policy and their lack of money by making policy in the form of mandates. Local officials have the same concern about state officials. They recently pooled their experiences in a report which predicts that state "unfunded requirements to local governments will only increase in the next decade as the intergovernmental roles of states as rule givers and localities as rule takers become firmly entrenched."

Local officials in many states have mounted systematic campaigns to reduce the impact of mandates, to prevent new mandates by fiscal note and reimbursement requirements, and to shift costly programs such as indigent health care to the state level. As with studies of federal mandates to states, there are studies reporting massive fiscal impacts of mandates. For example, a recent study in **New York** cites an estimate that mandates account for 71% of school district budgets and a range from 18% to 76% of county budgets. While rejecting these estimates as excessive, the study concludes that "the state is a major cause of local tax increases." It cites "nuisance" state mandates such as requiring towns to notify parking ticket scofflaws by certified rather than regular mail, limiting local dog license fees, and requiring New York City to pay unemployment compensation for volunteer workers.

The state record in dealing with mandates to local governments is mixed. On the one hand, there are major overall restrictions such as a 1991 **Louisiana** constitutional amendment permitting local governments to ignore unfunded state mandates. There is a similar statutory change in **Colorado**. On the other hand, many states have imposed new, federally encouraged restrictions on solid waste disposal, and a variety of state requirements ranging from records management in **Utah** to juvenile detention in **Montana**.

The Overall Impact Of State Policies: While it is too early to tally the score from state actions affecting local government this year, the pattern is likely to resemble the one found by Steven Gold in his assessment of 1991 actions. He found that "at least" 15 states reduced aid to municipalities and/or counties, cited only one major increase (**Pennsylvania** which paid for increasing aid with one of the largest tax increases in the nation), and found that at least a third of the states enhanced local ability to raise revenue. While stating that most states didn't single out cities and counties for especially harsh treatment in 1991, he concluded that states didn't do as much as he thought they should:

> *On the other hand, states did not do much to help local governments in any significant way either. The problems of cities and counties remained a low priority in most state capitols. States were so preoccupied with their own budget problems that local fiscal stress did not receive the attention it deserves.*

Local Responses: The initial impact of state actions in 1991 and this year on local government was muted in many states by two developments favorable to local finances. The first was fiscal relief from declining pension contributions. As states reduced their contributions for state employees because of improved actuarial outlooks and fiscal pressures, local contributions dropped as well. In some states, the same pension plan is used for state and local employees. In others, parallel changes were made in all state-administered plans, including those for local employees and teachers as well as those for state employees. Because of lags in assessment procedures, local property tax bases (based on assessed value) were often rising even as local property values were stagnant or even falling. Both these factors had primarily temporary effects.

As the temporary effects disappear, local officials have been making budget adjustments which have often been as substantial and as difficult as those of their states. These have been striking in **New York**, particularly in the major counties surrounding New York City, and in **Massachusetts** where local property taxes are limited by state law and local governments don't have the option of using local option sales or income taxes. In Cook County (Chicago area), the county board president blamed **Illinois** mandates for shortfalls in the county's nearly $2 billion budget, and recommended a county-wide sales tax that would raise sales taxes in Chicago (where customers would pay sales tax to the city, county, and state) to 8.75%.

The Outlook: The changes occurring in the past several years in state fiscal relations with local governments outside education don't appear to be the simple results of state fiscal problems but rather longer term trends accelerated by fiscal problems. With some notable exceptions, state policy seems to be moving in the direction of a sorting out of state and local roles. That sorting out discourages special state aid formulas to provide general revenues to local areas, even fiscally distressed ones, but encourages state takeovers of functions, like the movement to take over local Medicaid costs in **New York**, that bear most heavily on fiscally stressed jurisdictions. The trend discourages indirect local fiscal relief by eliminating or reducing special deductions for property taxes while increasing local fiscal options by new local taxing authority. Understandably, not all state and local officials are equally enthusiastic about such changes.

LOOKING FOR HEALTH CARE SOLUTIONS

State officials aren't giving up in their quest for health care financing solutions, but their journey isn't getting any easier.

Barriers To Dealing With Self-Insured Employers

Under the Employee Retirement Income Security Act (ERISA), states cannot directly regulate employer-provided benefits such as pension and health plans. States can regulate insurance of all types, so states have mandated minimum benefits (e.g., coverage of mental health and substance abuse) in health insurance plans. These mandates and state insurance premium taxes have caused employers increasingly to provide the substance of health insurance without its form, through what has become known as *self insurance*.

Employees see no difference between regular insurance and self-insurance. The benefits are the same and the claims processor is often an insurance company. But legally, self-insurance isn't insurance at all because the employer isn't buying protection against risk. The employer bears the risk that claims will be greater than anticipated, but reaps the gain if they are lower than anticipated. The plans don't require an insurance company, but those companies are often hired as claims processing agents, not as insurers.

The ERISA situation has made state-mandated benefits barely tenable. Large employers can avoid insurance while small ones need insurance to hedge against bad luck in the health of their employees. So the mandates are effective only for small firms. Small business leaders have sought relief from legislatures and, in an unknown number of cases, dropped insurance rather than providing the costly mandated coverages. In this situation, some states have adopted special encouragements for "basic" plans -- little more than positive rhetoric to cover exemptions from the mandates applied to small employers.

Besides eroding the effectiveness of mandated benefits, the ERISA situation has forced state proposals for universal health coverage to be packaged as "play or pay" plans, hung on the legal hook of state taxing power rather than state power to regulate. At a minimum, such plans would be subjected to major challenges in the courts.

A more immediate problem is the **New Jersey** holding that ERISA preempts surcharges on hospital bills to pay for indigent care (see Issue 12). The decision is on appeal. Meanwhile, legislators briefly extended the Uncompensated Care Trust Fund to give themselves enough time to decide what to do. Two **Connecticut** employers, Hewlett Packard and Pepsi Cola Allied Bottlers, have initiated similar litigation in that state. Several other states, including **Massachusetts**, have comparable plans. State officials are worried that future ERISA-based challenges could threaten the newly enacted **Minnesota** plan for uncompensated care. Other state policies, such as **New York**'s differential hospital charges, are also at risk and perhaps even some Medicaid provider taxes.

These concerns were serious enough to send a delegation of 14 governors to the White House in late June to attempt to convince Bush Administration negotiators to back some form of exemption legislation in the Congress. Neither major business groups nor the Administration has shown much enthusiasm. They oppose the state mandates of services, don't like proposed state health financing plans that appear to put more money into health care without addressing cost control, and some are concerned about taxes on health insurance. Prospects for Congressional action before November are miniscule.

Never Give Up

Despite the massive obstacles to single state universal health plans, many legislators support such plans. In June, the **New York** Assembly passed one. It provides a common plan to replace Medicaid and private health insurance as well as cover the uninsured. Funding would come from a 10% payroll tax (8% on employers, 2% on employees) plus a special tax on unearned (non-wage and salary) income. The measure passed on a party-line vote, viewed by the Democrats who supported it more as an attempt to dramatize the issue than pass legislation this session. The Senate Republican leaders say they will soon have a plan of their own with different financing.

A blue ribbon group in **Montana**, Health Care for Montanans, has rejected universal care on a state-by-state basis on the grounds that the medically uninsured with substantial health problem would flock to a state that provided it. It is pushing more modest suggestions, including medical malpractice reforms and an attempt to become the first state in the nation to adopt a uniform electronic billing system.

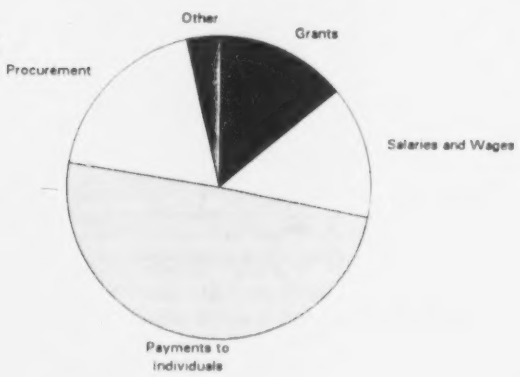
FEDERAL IMPACTS ON STATE FINANCES

For at least the remainder of 1992 it appears that federal policy changes will have little impact on state finances for the simple reason that few changes in federal policy appear likely. Most of the current action is in Medicaid reimbursement decisions. The situation is likely to change next year as federal officials get more serious about budget cutting, particularly in defense, and about new mandates.

Coveting Federal Payrolls And Contracts

The impact of federal procurement and payrolls on state economies is so substantial that many states have special programs to attract and retain federal installations and to assist firms in their quest for federal contracts.

Percentage Distribution Of Federal Spending Attributable To Individual States, FY 1991



As shown by the pie chart, federal payments for individuals (see Issue 12) dwarf the significance of payrolls and contracts. But large amounts are involved. In FY 1991, federal procurement awards amounted to $811 per capita. In nine states, over $1,000 per capita came from federal purchasing decisions.

Wage and salary payments to federal employees have nearly as large an impact. Those payments were $611 per capita nationwide in FY 1991. The federal payroll was over $2,000 per capita in **Alaska** and **Hawaii** and over $1,000 per capita in **Maryland** and **Virginia**.

Federal Purchasing, State-By-State

Federal purchasing decisions have highly uneven impacts among the states. The top-ranked state has per capita amounts nearly eleven times those of the lowest-ranked state. Eighteen states capture procurement dollars that are less than half the national average. There appears to be a minimum amount of federal purchasing associated with local purchases of post offices, military recruiting stations, and IRS offices. Nine states, with per capita purchases of $200-300, appear to get little more than this level.

Per Capita Federal Procurement Awards, FY 1991

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	New Mexico	$2,237	17	Utah	$810	34	North Dakota	$383
2	Connecticut	1,621	18	Mississippi	795	35	Georgia	377
3	Virginia	1,585	19	Texas	758	36	West Virginia	348
4	Maryland	1,519	20	Washington	711	37	Illinois	344
5	Alaska	1,413	21	Hawaii	670	38	Oklahoma	325
6	Missouri	1,412	22	Ohio	611	39	North Carolina	320
7	Colorado	1,367	23	New Jersey	592	40	Wisconsin	303
8	Massachusetts	1,360	24	Florida	563	41	South Dakota	302
9	California	1,057	25	Kentucky	550	42	Nebraska	299
10	Idaho	984	26	New York	547	43	Wyoming	294
11	Tennessee	984	27	Louisiana	507	44	Delaware	279
12	Maine	938	28	Minnesota	478	45	Iowa	258
13	South Carolina	911	29	Rhode Island	460	46	Michigan	246
14	Nevada	882	30	Kansas	457	47	Montana	240
15	Alabama	846	31	New Hampshire	453	48	Oregon	219
16	Arizona	826	32	Indiana	436	49	Vermont	210
	United States	**811**	33	Pennsylvania	402	50	Arkansas	205

The key to a high ranking is to have major federal contractors oriented to defense procurement, like **Connecticut** and **Missouri**, or a specialized function, like atomic energy in **New Mexico**, or a combination such as defense and health-related federal activities in **Maryland**. The states most at risk from a cutback in federal spending are probably those with high dependence on defense contracts. The most vulnerable are **Connecticut** ($1,500 per capita in defense contracts in FY 1991), **Missouri** ($1,213), **Massachusetts** ($1,149), **Virginia** ($1,064), **Alaska** ($973), and **Maine** ($851).

Federal Payrolls, State-By-State

The table (next page) shows the wide range of impacts of federal payrolls on the states. The per capita payroll was more than nine times as high in **Alaska** as in **Wisconsin**. Four states are more than twice the national average. Three states are less than half of it.

A portion of federal payrolls is related to functions that must closely approximate population, such as delivering the mail and collecting taxes. These activities seem to set a base of about $250 per capita, which is about all the federal payroll to be found in **Iowa**, **Michigan**, and bottom-ranked **Wisconsin**. The remainder of the federal payroll is primarily related to the location of federal facilities, such as military bases, and to federal activities that are by their nature unevenly distributed among states such as administering agricultural subsidies and federal land holdings.

Per Capita Federal Wages And Salaries, FY 1991

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	Alaska	$2,236	18	Kentucky	$663	34	Massachusetts	$470
2	Hawaii	$2,042	19	North Carolina	636	35	New Jersey	454
3	Virginia	$1,805	20	Nebraska	624	36	Pennsylvania	439
4	Maryland	$1,334		**United States**	**611**	37	Tennessee	437
5	Colorado	945	21	Delaware	611	38	Illinois	432
6	New Mexico	921	22	California	610	39	Oregon	420
7	Utah	840	23	Missouri	587	40	Arkansas	409
8	North Dakota	838	24	Rhode Island	576	41	Connecticut	396
9	Georgia	781	25	New Hampshire	568	42	Vermont	387
10	Washington	779	26	Texas	568	43	New York	376
11	Oklahoma	773	27	Arizona	566	44	Ohio	374
12	South Dakota	740	28	Nevada	544	45	West Virginia	357
13	South Carolina	730	29	Florida	524	46	Indiana	339
14	Alabama	714	30	Mississippi	517	47	Minnesota	317
15	Kansas	714	31	Idaho	502	48	Iowa	278
16	Wyoming	703	32	Louisiana	490	49	Michigan	270
17	Montana	671	33	Maine	470	50	Wisconsin	249

Federal Contribution To State Fiscal Stress: A recent report from the Center for the Study of the States concluded, as **Reports** does, that federal aid cuts *are not* the source of current state fiscal problems -- though other federal actions and inaction are major problems. The report comments:

> *Federal policies have contributed considerably to recent state fiscal stress in a variety of ways. The most important effects occurred through the Medicaid program -- the fastest growing part of state budgets -- and the recession, which depressed revenue and increased welfare and Medicaid spending.*
>
> *Federal aid reductions have not been an important source of recent state fiscal stress... Federal policies have affected state finances in several other ways -- through tax policy, new unfunded mandates, and the federal failure to cope effectively with problems like health and poverty. Federal court rulings have also caused budget problems (as have state court decisions).*

The latest data from the national income accounts show that federal aid to state and local governments rose 14.5% from the first quarter of 1991 to the first quarter of 1992. During the same period, state and local receipts from their own sources (e.g., taxes and user charges) rose by much less, 6.2%.

Recent attempts to make major changes in federal fiscal patterns have failed. Proposals for massive new urban aid programs and recession-fighting infrastructure aid have become urban aid packages that simply increase funding for some existing programs and expand enterprise zones. The balanced budget amendment, which under some scenarios could result in major cutbacks of federal grants, is making little progress in the Congress.

Federal Mandates And Preemption: This has been a relatively quiet year for Congressional action on mandates to state and local government. There are, nonetheless, many examples of mandate activities: (1) affordable health care proposals that would restrict state ability to mandate benefits and, in the President's proposal, threaten state insurance premium taxes on health insurance, (2) preemption of aspects of state utility regulation and new building code mandates in the pending energy legislation, (3) restrictions on state revenue-raising flexibility and new penalties to be imposed on states in reauthorization of the Resource Conservation and Recovery Act, and (4) cost-increasing regulations associated with the Americans with Disabilities Act.

Medicaid And Politics: The increasingly widespread use of Medicaid bootstrap financing devices and state claims for retroactive Medicaid reimbursement seem to have made some federal Medicaid decisions increasingly political, in appearance if not in substance. The most obvious current case is **New Jersey**. Legislative leaders (R) there were working with the White House for what amounts to direct inputs to the pending budget. The culmination of the process occurred in late June when the leaders announced that an additional $84 million in retroactive payments would be available. They immediately allocated the money to reverse some of the cuts in their budget package, such as raises previously negotiated with unionized workers. Democrats proposed an alternative use, restoring cuts made in the homestead rebate program.

MISCELLANY

Legal Challenges To Higher Education Spending

We may have to call out the National Guard because I'm just not going to do it.

On reflection, Governor Fordice decided this wasn't something that a **Mississippi** governor should be saying in 1992 about federal desegregation orders. It evoked strong memories of a prior governor standing at the schoolhouse door to block desegregation in the 1950s. The corrected version from the governor's press secretary is: "We don't need the {federal} interference to any degree in trying to tell us how to spend what little monies that we have in Mississippi."

Southern officials may have less to worry about than officials of states like **California**, **Illinois**, and **New York**. A new line of cases may do to state funding of universities what the equalization suits have done to public school funding. This was little noticed in the larger states until a suit was filed in **New York** in February that relies on the same legal principles at stake in the cases in **Alabama**, **Mississippi**, and **Texas**.

Desegregation In Southern Universities: Through the 1950s the states of the Old Confederacy maintained racially separate public higher education systems, effectively baring all or all but a few token blacks from white schools. The black schools were generally inferior in facilities, budgets, academic reputations, and achievement levels of students before admission and after graduation. There were a few cases of "separate but equal" higher educational institutions in the North, but not whole university systems as in the South.

A combination of compliance with desegregation laws, policy preferences, and the politics of holding power in states with large percentages of black voters essentially eliminated discrimination against students by race. For decades, a black Mississippi resident has had an equal or better chance of admission and graduation from the flagship institutions as an equally qualified white resident.

Equal Access Doesn't End The Debate: One could argue, as Mississippi and other states did, that equal or better-than-equal access for students should end the issue. Federal officials didn't accept this view. In some Southern states, they tried to promote more integrated institutions than unfettered student choice alone would provide. Mississippi provided an ideal environment because the formerly white flagships are away from the major center of population growth in Jackson. It is served by Jackson State, a formerly black institution. By blocking expansion of the flagships in the Jackson area, the courts could create a monopoly market for Jackson State, thereby encouraging whites to attend it.

These strategies didn't work for regional four-year institutions that were the growth products of junior colleges and teachers colleges throughout Mississippi and other states. There the formerly white institutions proved a stronger draw for both black and white students with funding for operations more or less following enrollment and funding for new buildings more or less following enrollment growth. At this point, Mississippi and similarly situated states could argue that: (1) students had choices unfettered by discrimination, (2) the formerly white schools were in fact integrated, and (3) the allocation of funds among schools was color-blind or, in many cases, biased toward the formerly black institutions. Various other adjustments were being made, such as adjusting university governance in Louisiana to wipe out the vestiges of separate black and white systems.

Funding Disparities In the North And West: While this was occurring in the South, Northern states were dealing with their problems of having flagship universities not serving urban centers by (1) permitting flagships to establish branches and professional schools in the centers, (2) accepting state responsibility for formerly municipal systems such as New York City's system, (3) providing extra aid to private institutions in urban centers, such as the University of Pittsburgh and Temple, and (4) creating new major institutions to aspire to flagship status, such as Cleveland State and the University of Illinois (Chicago). Some newer institutions such as state institutions in Northern central cities and along the Texas-Mexican border inherently tended to have predominantly minority students.

Developments In The Courts: The Mississippi case drew national attention even before it was decided by the U.S. Supreme Court in June. Last October, President Bush directed the Justice Department to withdraw its brief supporting Mississippi and to argue the case against the state's position. The new federal position prevailed in an 8-1 Supreme Court decision in June. The case will now go back to lower courts where the question of what Mississippi must do will probably be litigated for years. A similar case in Alabama has already produced larger budgets for the predominantly black institutions, but more litigation may occur there and in other states.

The Mississippi case involved unwinding a history of segregation but the cases in **New York** and **Texas** don't depend on that factor. The plaintiffs contend that the City University of New York, with predominantly minority students, receives less per pupil than the State University of New York with predominantly non-minority students. Both the legal principles and the facts are at issue. While SUNY gets more aid per pupil, much of the differential, perhaps all, may be explained by the concentration of high cost medical and other professional programs at that institution. In the Texas case, the funding differentials between the South Texas institutions (with mostly Hispanic students) and the University of Texas are similar to those between flagship and regional institutions in other states.

The New York case is in trial court. The Texas case is on appeal. Other states will likely experience similar litigation, following the pattern of the public school finance equalization cases. The "years of litigation-driven confusion and destabilization" predicted by Justice Scalia's dissenting opinion in the Mississippi case do appear likely.

Rating Professional Licensing Boards

Oklahoma and **North Dakota** do four times better than the national average in regulating physicians while **Massachusetts** and several New England states do half as well. This conclusion, and ones like it for licensing boards in other regulated professions, can be reached from data regularly published by associations of state agencies such as the Federation of State Medical Boards.

These associations don't rank their members. They do provide comparable statistical information on such subjects as the number of regulated professionals in each state, the number suspended or otherwise disciplined, and the budgets of the agencies. Some consumer groups, such as the Public Citizen Health Research Group, convert these data into rankings, usually on the theory that the more disciplinary actions taken, the more effective the licensing agency.

The licensing agencies aren't comfortable with these rankings. The approach is comparable to comparing state highway patrols by the number of tickets written rather than by accident rates or average highway speed. But the rankings can have an impact, particularly when combined with well-publicized disciplinary situations. This recently happened in **Massachusetts**. The nationally publicized case involved a female psychiatrist whose sexual relationships with a patient allegedly led to his suicide.

In Massachusetts, as in many states, the fees paid by doctors and other professionals for their licenses to practice enter the general fund. Operating expense appropriations for regulation are often less than the fees. Groups representing the licensed professionals often lobby for earmarking of fee revenue for the regulatory agency, reasoning correctly that this would provide a natural limit on the level of fees. State fiscal officials often reject this approach because of objections to earmarked revenues generally and potential revenue losses in particular cases. Reforms announced by the governor in Massachusetts involve raising physicians' fees and earmarking the revenue for regulation while leaving the general fund with a large cut of current fee revenue.

Water Supply Projects

Throughout the West and in limited circumstances East of the Mississippi, the federal government operates major systems of dams and reservoirs without which irrigated agricultural activity and even urban development in arid states would be massively less significant than it is. The state role in these projects has usually been limited to parkland development and dealing with fishing and recreational uses. The big trade-offs -- like whether water goes to agriculture or urban development and whether flows are maintained for fish rather than keeping water stored for irrigation -- are federal choices.

Two developments are encouraging greater state interest. The first is that the federal budget isn't providing for much new investment. The second is that there are strong pressures in the Congress and the federal executive branch to change some of the rules in ways agricultural interests view as unfavorable.

One sign of interest is the continuing effort in **North Dakota** to put up large sums of state money for state-funded water development. The proposal was seriously considered in the legislature and may be put on the ballot by initiative.

Another sign of interest was the February announcement by Governor Wilson that he wants **California** to take over the Central Valley Project from the federal Bureau of Reclamation.

Access to water in the West has been a source of controversy since settlement began, as any reader of Western novels can attest. A new 141-page study by the Advisory Commission on Intergovernmental Relations concludes that water problems are largely problems of coordination and management, rather than problems of scarce supply. Access problems also affect the East. For example, **Alabama** officials are concerned with **Georgia**'s interest in diverting water from rivers that flow into Alabama. A water planning bill was proposed by the governor to establish an agency to deal with the situation, but wasn't adopted in the recently concluded legislative session.

Also Noted: The Federation of Tax Administrators has done a survey of revenue estimating procedures and organizational responsibilities in the 50 states. Results appear in Tax Administrators News (March and earlier issues). Governor Weicker collected a courage award worth $25,000 from the John F. Kennedy Library Foundation for his role in enacting the new **Connecticut** income tax. His comment: "I'm not in the courage business, I'm in the governing business." **Oklahoma** acted this year to maximize use of federal funds by converting its sales tax relief from a refundable income tax credit into a supplement to cash welfare assistance, thereby making it a welfare payment eligible for cost sharing.

West Virginia is nearing the end of its attempts to recover an estimated $257 million in securities trading losses incurred by its investment of pooled state and local cash balances. It has recovered $28 million from settlements with securities firms, won $32 million (plus interest) from Morgan Stanley in a trial court decision being appealed, and has a $14 million case left against Chase Securities. The legal bill will be substantial. **Iowa** is less advanced in attempts to recover about $75 million for its pooled investments. The Iowa case clearly involves fraud by private firms with state errors in the selection and supervision of firms. The West Virginia case involves excessively risky practices by state officials, but no allegation that the firms or their employees absconded with any money. Even the best conceivable legal outcomes will leave state and local governments in both states with massive losses.

The process of states getting out of the business of insuring financial institutions -- savings and loans, banks, industrial banks, and credit unions -- also appears to be nearing an end after the big hits taken by taxpayers in **Maryland**, **Ohio**, and **Rhode Island**. The most recent state to take a loss is **Pennsylvania** which will be terminating the Pennsylvania Deposit Insurance Corporation. One of the three remaining covered banks has joined the Federal Deposit Insurance Corporation while the state has seized the other two. Money in the state Workers' Compensation insurance fund will be used, with no immediate general fund impact. The fund will temporarily own the banks.

TECHNICAL NOTES

State Finances: Two recent additions to the literature of privatization are Edward Hudgins and Ronald Utt, eds., How Privatization Can Solve America's Infrastructure Crisis (Heritage Foundation, 214 Massachusetts Ave., NE, Washington, DC 20002) and Reinvigorating The Public Service (Public Employee Department, AFL-CIO, 815 16th St., Washington, DC 20006). The second volume reflects efforts by public employee groups to show that gains in service delivery don't depend on who does the delivering. A section of Governing (May) includes a directory of "Who's Who in Privatization," assesses privatization in four fields, and concludes, "The privatization trend shows no signs of slowing."

The NASBO survey is State Balanced Budget Requirements: Provisions and Practice (June). PARI (212 Carnegie Center, Princeton, NJ 08540) summarized its cost-cutting recommendations in its Public Affairs Focus (June). The Ohio Operations Improvement Task Force (77 S. High St., Columbus, OH 43266) issued its report in November as Bringing Out The Best In Ohio. The Maine recommendations are found in Legislative Document No. 2330. The table on comparative earnings growth was developed by **Reports** from data appearing in the Survey Of Current Business (April).

Local Finances: The National League of Cities (1301 Pennsylvania Ave., NW, Washington, DC 20004), produced State Mandates: Fiscal Notes, Reimbursement, And Anti-Mandate Strategies. The 78-page report includes tables detailing each state's fiscal note and mandate-limiting laws. The New York study is Taking The Credit & Shifting The Blame (The Empire Foundation, 301 Hamilton St., Albany, NY 12210). Gold's assessment, State Policies Affecting Cities And Counties In 1991, was recently published by the Center for the Study of the States (411 State St., Albany, NY 12203).

Federal Impacts: The report, The Federal Role In State Fiscal Stress is also from the Center for the Study of the States. NCSL's monthly Mandate Watch List, provides a detailed running tabulation of mandates and preemptive legislation pending in the Congress. For a good summary from a state perspective, see "U.S. Adds Programs With Little Review Of Local Burdens," New York Times (3/24).

Water Supply: The Advisory Commission on Intergovernmental Relations (Washington, DC 20575) study is Coordinating Water Resources In The Federal System: The Groundwater-Surface Water Connection. For a summary of California's continuing controversies, see California Journal (June).

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Correction, Tennessee Health Provider Taxes: The Issue 11 characterization of Tennessee's new tax on health care providers got the economic effects right but the law wrong. The tax changes appear to provide a broad-based new tax on health and non-health activities. But the non-health activities escape added taxes by repeal of the old taxes on them, not by a credit against the old taxes.

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Editorial Note: To end the bias of writing about state policies from a Washington area location, **Reports** editor Hal Hovey has relocated to Columbus, Ohio. The editorial office remains in Virginia (new address and phone in box below). There is no change in the subscription office.

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STATE POLICY REPORTS

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IN THIS ISSUE

Escalating costs keep health care financing at the top of state agendas. But there hasn't been much progress in making health care more affordable. Major reform measures passed this year by four states offer only slow changes. Fiscal problems preclude significant taxpayer subsidies of health care. There is considerable interest in plans that underwrite insurance for the hard-to-insure with premiums from other insurance customers.

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- State Health Insurance Reforms Are Popular p. 3

Cost pressures are forcing consideration of Medicaid cost cuts and new provider taxes. The taxes are more popular than the cuts because officials of many states fear cuts would just shift costs to other programs and private insurance.

- Medicaid Cuts Are Hard To Find p. 6
- Provider Taxes Catching On p. 9

With lotteries showing little growth, states are betting on new forms of gambling. More casinos are likely to be approved. Some lotteries are offering about the same betting opportunities as popular casino games.

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This election-year summer, most states are postponing budget adjustments. Higher education is the big loser from fiscal stringency.

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- Higher Education Taking Big Hits p. 19

A note contrasts conventional economic wisdom with assertions about impacts of gambling. Technical notes cover new information on health care finance and detail sources and caveats.

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July 1992 (Second Of Two July Issues)

DEVELOPMENTS IN HEALTH CARE FINANCING

State officials continue to look for health care financing solutions that offer dramatic results but don't drain tight budgets. **The search isn't producing much.**

HEALTH CARE ISSUES HEAT UP IN STATEHOUSES: Kansas, Missouri Legislators Wrestle With Bills. Action Unlikely -- headline Kansas City Star (3/13)

Tight state finances have slammed the brakes on proposals that depend upon state subsidies or tax credits to encourage expansions of health insurance. Expansion by mandating private coverage is stalled by two massive obstacles. The first is the federal Employee Retirement Income Security Act (ERISA). As discussed in Issue 13, it provides a major impediment to new state plans and jeopardizes some existing state programs which spread the costs of the uninsured over all health care consumers. The second is the reluctance of state officials to raise taxes on anyone and particularly on employers in competition with those of other states and nations.

The lack of progress is evident in a new book assessing state options for improving access to health care. It examines the alternatives considered by a governor's task force in Michigan that reported in 1990. The same list of options is considered by similar task forces in other states. The editors conclude:

> *Since then, a major recession has struck Michigan and many other states. State budget deficits have soared, as has the federal budget deficit. Most states are struggling to fund the expansions of the Medicaid program mandated by the federal government during the late 1980s and have backed away from new initiatives to improve access to health care. ... In Michigan, tight state finances have led to a backward movement on health care access improvement through the elimination of the General Assistance program. Other states have taken similar measures.*

This report concludes: "The dire financial predicaments of many of the states have clearly shifted the focus of health care reform back to the federal level." But what little action is developing in Congress this year is devoted to apparently costless ways to increase the availability of care by such devices as insurance regulation and tort law reform.

Most state officials continue to favor the federal actions suggested in a new report by the Advisory Commission on Intergovernmental Relations. They include federal takeover of nursing home costs, 100% federal payment for new federal mandates, greater state flexibility in administering Medicaid, and comprehensive health care reform as a national, not state, responsibility. The report also echoes a point constantly made by state officials about the limitations on what they can accomplish through the Medicaid program:

Modifications to Medicaid will yield only marginal improvements in the health care system because Medicaid accounts for only 12% of all health care expenditures. Without effective methods of cost containment, any improvements in Medicaid's efficiency and effectiveness resulting from these improvements may be wiped out by rising costs.

STATE HEALTH INSURANCE REFORMS ARE POPULAR

Legislation and/or administrative action to "reform" health insurance is being discussed in practically all states, and implemented in many. **The objective of the reforms is to improve the position of a relatively small target group with big problems in getting or paying for coverage.** Typical target groups are: (1) uninsurable persons, such as those with chronic diseases, (2) transitional situations, such as persons changing jobs or employers changing insurance carriers, to prevent loss of coverage because the new carrier won't cover preexisting conditions, and (3) individuals and small businesses facing sharp premium increases because of high past claims.

The reforms often are discussed as though there were no costs involved. The situation parallels other cross-subsidies such as "lifeline" and "basic service" utility rates. The reforms parallel assigned risk plans in auto and fire and casualty insurance and bars against life and auto insurance underwriting criteria viewed in some states as bad public policy (e.g., age, sex, location of residence, past auto or health claims).

With no new money on the table, higher rates for those without the targeted problem finance lower rates for those with the targeted problem.

The claim is often made in state debates that companies will absorb the costs of controlled rates for target groups. But legislation seldom contains the teeth required to support this claim. As a result, many of the plans have been backed by some insurers, suggesting that relief for the target groups will come from other insurance customers rather than company profits.

Occasionally, claims that insurance companies will absorb costs have been backed by legislative requirements, such as those of Proposition 103 (auto insurance) in **California**. The result then becomes litigation over whether the legislation is an unconstitutional taking of private property and threats that companies will reduce the availability of insurance. The ultimate reduction is company withdrawal from the state, a problem **Vermont** is currently experiencing with health insurance carriers.

The newest experiment is "community rating" (as distinct from rating individual persons and small employers). One such plan becomes effective in **New York** in April 1993 as a result of recent state legislative action.

New York has traditionally maintained a two-tiered health insurance market. Blue Cross/Blue Shield, with 2.1 million subscribers, has been taking many of the higher risk cases while private insurers have captured the lower cost group policy market. To attempt to keep the system tenable, the Blues have been getting state-backed breaks in taxes and hospital costs. Notwithstanding these, the Blues' situation was becoming untenable, with a massive rate hike considered the alternative to the legislation that passed.

Although there was debate over how large the effect would be, there was general agreement that private insurance rates would tend to rise. Insurers claimed large increases would be likely. For example, a Prudential spokesperson predicted rate increases for 70% of its small business customers with the average rate increase in the 20-50% range. Proponents of the legislation pointed to the ability of insurance regulators to control these increases.

After the legislation passed, there was not a mass announcement of companies pulling out of the state. This was good news for the availability of coverage but bad news for costs to consumers. It suggests the companies believe they will be able to pass along higher costs. If so, the legislation will work as a cross-subsidy, making health insurance more available and cheaper for higher risk customers but more expensive for lower risk customers, just as community rating works for auto coverage. The higher costs will unquestionably cause at least one employer to drop health insurance and others to reduce coverage by devices like benefit caps, higher deductibles, more copayments, and larger employee contributions. There is no way to estimate reliably the magnitude of these effects.

State Health Notes (7/13) considers **Maine**, **Oregon**, and **Vermont** the only other states with community rating, "though their laws are less far-reaching than New York's." With most of the legislatures not now in session, the state with the most lively prospects for further 1992 action is **Ohio**, where substantially different House and Senate bills are now in conference committee.

The contrasts between sweeping plans to extend health care coverage and modest changes in existing insurance arrangements are most obvious in **California**. Many varieties of universal care have been offered in the legislature. The California Medical Association has been pushing a ballot initiative to mandate employer coverage. Governor Wilson opposes these in light of the state's economic problems: "The last thing in the world we need to do to small business in California is add to their cost burdens."

His proposals include pooling small business insurance purchasing power, limited regulation of rates charged employers with between five and 25 workers, limiting insurers' ability to delay coverage for pre-existing illness and to refuse to renew policies, covering workers who change employers, changing prohibitions against corporate practice of medicine to let hospitals employ doctors, creating a uniform billing form for all insurers, and preventing physician conflict of interest in referrals of patients to testing and other facilities in which physicians have ownership interests. The elected California insurance commissioner, who has a more extensive proposal of his own, calls the governor's plan "lowest-common denominator politics," and "creeping incrementalism." He argues it "offers Band-Aids when our health care system needs major surgery."

State subsidies for private coverage are proving unpopular. To avoid having the plans to provide new or cheaper private coverage become zero-sum games among premium payors, states must bring new money to the table in the form of subsidies of private coverage either through direct expenditures or tax expenditures. New plans to do this anytime soon didn't go far this year. **Florida**, **Minnesota**, and **Vermont** have enactments with scheduled future implementation. New proposals involving use of state resources are constantly appearing. For example an **Idaho** task force on the uninsured recently reported with recommendations for expanding Medicaid and tax incentives for employer plans.

The Florida, Minnesota, and Vermont plans are mostly plans to make plans, not plans to do something specific. As the Burlington Free Press (2/9) commented on Vermont's plan, "There will be skirmishes at every crossroads ... as the health care authority begins to design the universal access plan." The Boston Globe (7/6) described the plan in glowing terms -- "the most far-reaching health reform legislation ever enacted by any state" -- but followed with the words that become the death knell of reform plans covering taxes, school finance, insurance, and health care: "**The details have yet to be worked out.**" USA Today (5/13) said the Vermont law "does little more than promise to do something in the future." The Minneapolis Star-Triune (5/17) counts Minnesota's new HealthRight plan as creating 13 commissions, boards, task forces and committees, requiring the hiring of 116 staff personnel, like analysts and auditors, and calling for 33 studies and reports.

Past enactments aren't fairing well. **California** continues to postpone its tax credit for employers newly providing coverage. The much touted **Massachusetts** universal plan of 1988 isn't dead, but its "pay or play" requirement now is deferred until 1995. The Bay State had several transition demonstration programs with state subsidies of private coverage for hard-to-cover groups. They were terminated in April. **Georgia**'s pool concept (enacted in 1989) was based on agreement on the rate ceiling of a maximum of 50% above base rates, but no agreement on how to pay the excess. Hospitals balked at a surcharge on hospital stays. Insurers balked at a surcharge on premiums. The governor and key legislators balked at a state subsidy. So the plan hasn't been implemented.

The alternative to states bringing new money to the table is to take some benefits off the table. Many of the reforms do just this by exempting small employers from past state mandates of coverage, such as for mental health. **Florida**'s new legislation is one of many examples. As of April, the "basic benefit plans" were being marketed in 10 states: **Illinois**, **Kentucky**, **Maryland**, **Missouri**, **Montana**, **Oklahoma**, **Oregon**, **Rhode Island**, **Virginia**, and **Washington**.

The state reforms are showing limited results, but the situation could change. A recent General Accounting Office report (Access To Health Insurance: State Efforts to Assist Small Business) summarized the situation:

> *Because of the difficulties in marketing new insurance policies to small firms and because most of the reforms have been introduced during the recession, it is too soon to tell whether the reforms will increase insurance coverage. Budget problems are limiting states' ability to adopt reform measures requiring substantial state subsidies or funding. As a result, states are tending to focus on reforms involving little or no cost to the state treasury. These reforms attempt to correct several serious problems in the market but have yet to significantly increase the number of small business employees with health insurance.*
>
> *Initiatives requiring state subsidization of the small business market are rarer, tend to be limited in scope and duration, and have produced limited results. Attempts to lower the cost of insurance by waiving state-mandated benefits have also produced only modest employer responses. Ultimately, small business market reforms may do little to make health insurance more affordable because they do not address the underlying growth in health costs.*

MEDICAID CUTS ARE HARD TO FIND

Cost-Cutting Options: Through all of the budget-tightening of 1992, there have been few real cuts in Medicaid programs. To save big money in Medicaid, states would need to do one or more of the following: (1) cut the number of people eligible for services, (2) cut the list of available services, (3) cut the prices paid per unit of service, (the reimbursement rates), (4) effectively steer patients from high cost to low cost services and/or from high cost to low cost providers, and (5) require Medicaid recipients to pay more for the services they receive, (copayment).

Eligibility Restrictions: Eligibility for Medicaid is largely controlled by eligibility for cash assistance programs, like AFDC, and by federal mandates increasing eligibility for pregnant women and young children. The tendency in cash assistance programs has been to freeze payment levels, but not to reduce the standard of need that determines eligibility. The state medically indigent programs, for those not on cash assistance programs, have generally survived through a combination of perceived federal mandates and fear that restricting eligibility will just substitute costs without federal cost sharing (e.g., indigent care, hospital bad debt) for the same costs now being shared with the federal government.

Proposals for eligibility restrictions affecting nursing home recipients under medically needy programs have met with massive reluctance. No one wants to kick current residents out of their nursing homes. One such plan, in Governor Weld's cost-cutting recommendations for **Massachusetts**, now has been dropped. Governor Thompson dropped a proposal to extend **Wisconsin**'s cost-cutting plan to home health care. **Oklahoma** dropped proposed eligibility restrictions this spring in face of a threat that 6,000 nursing home residents would be thrown into the streets.

> *It's elbowing out almost everything else in terms of growth. This is the gorilla that's out there. This is the Pac-Man, eating everything up. Wisconsin's social service secretary on the impacts of Medicaid, (Milwaukee Journal, 3/15)*

Texas officials decided to absorb the scheduled eligibility increases (to 185% of the poverty level) for pregnant women and infants ahead of the schedule required by federal mandates. In a reverse move, **Idaho** decided to drop some previously planned expansions of eligibility for the medially indigent. In **California**, the governor's early-July proposals to resolve the budget crisis included limiting Medi-Cal eligibility to legal aliens and citizens, eliminating substantial costs for illegal aliens.

One area of restricting eligibility showing intense activity is the prevention of higher income elderly persons from impoverishing themselves to become eligible for Medicaid. These proposals are part of a newly announced governor's plan in **Ohio** and have been adopted in one of many available forms by an uncounted but substantial number of states.

Service Reductions: A major barrier to eliminating coverage of optional services is that many states don't provide them now. The most activity appears to be in cutting optional services in states that have them, such as certain forms of dental and optical care. The governor's mid-June proposal would drop many of California's optional services including acupuncture, dental care, chiropractic services, podiatry, and psychological counseling.

Rate Cuts: There have been two massive institutional barriers to cutting reimbursement rates: (1) fear of litigation under the Boren Amendment and (2) desires to make deals with providers swapping higher reimbursements for support of provider taxes.

Medicaid rates are often well below private and Medicare rates. This raises concerns that at current rates most services will become unavailable in rural areas and pre-natal care may become unavailable anywhere. Where reimbursement rate changes are occurring, they aren't necessarily cost-saving measures. For example, **Texas** has been emphasizing preventive care by lowering rates for anesthesiology and radiology, but raising rates for primary care physicians.

Shifts To Lower Cost Providers Or Services: Nearly every state is discussing the cost-cutting potentials of: (1) diverting potential nursing home patients to home health care, (2) diverting routine cases from emergency rooms to physicians' offices, and (3) managed care. However, budget officials have been reluctant to count savings from these measures, as each contains significant potential to increase costs by greater utilization.

Copayments: The concept of copayments being made by people who, by definition, lack the ability to pay has never been an easy sell to legislators. The new copayments are generally too small (e.g., a dollar per physician visit) to have much of an impact on bottom line Medicaid spending. Nominal copayments aren't popular with providers. The cost of collecting and accounting for them can exceed the value of the copayment. It is also realistic to expect that the providers themselves will make many of the copayments theoretically being required of Medicaid recipients.

Phony Savings: The most popular claims for cost cutting in Medicaid aren't cost cuts at all. Continuing past practice, many states are appropriating less than the predicted costs of current services and calling the difference savings. These are likely to appear as supplemental appropriations later in the year. The rationale for the reductions takes forms like requiring unspecified savings to be realized by later administrative action and/or by better management.

Popular Ways to INCREASE Medicaid Costs: Medicaid budgets, but not necessarily total state and local indigent health spending, are being increased by decisions to move large numbers of people out of 100% state and local indigent care programs and onto Medicaid to gain the advantage of federal cost sharing. Examples are special programs for general assistance recipients, state-funded subsidies for indigent care that serve some persons who could be qualified for Medicaid, public health programs, activities in state facilities for the mentally retarded, and substance abuse programs.

Organizations of state officials aren't discouraging such activities, though they increase Medicaid spending. For example, in May the National Governors' Association released a report, Outstationing Medicaid Eligibility Workers At The Community And Migrant Health Centers. "Outstationed" eligibility workers are to the number of Medicaid recipients the equivalent of what "Avon-calling" personnel are to cosmetic sales.

Because provider tax revenues are typically off-budget, raising provider taxes cuts on-budget spending increases. This effect has been explicitly claimed as savings and budget cuts in some states, such as **New York**.

Most states are looking to ways to expand Medicaid to cover 100% state-financed costs and to cut Medicaid fiscal impacts by provider levies rather than looking for ways to cut Medicaid outlays. The result is a substantial state bet that federal policy will not be changed soon. The stakes are high, accounting for a large portion of the $10 billion federal supplemental appropriation needed in the federal FY 1992 budget for Medicaid.

The state stakes in current federal Medicaid policy are becoming larger by the day. Many state officials worry about the prospects, even as they expand their reliance on the program. The Maine Telegram (2/9) captured many of the worries in a feature entitled, "Medicaid: A 'House of Cards'." The head of the mental retardation agency, who now gets 40% of his funding from Medicaid, called the situation "a mixed blessing" because "your vulnerability continually increases as you draw down more federal dollars." A deputy in the Maine human service agency called plans to expand Medicaid "reasonable and sound," but continued:

> *I'm not confident that anything in the federal budget is safe. If they pull the rug out from under Medicaid, you're going to have 50 states filling for Chapter 11 bankruptcy protection.*

An exception to the general reluctance to cut Medicaid may be **Wyoming**, at least according to April's State Health Notes. It indicates that the state: (1) limited inpatient hospital coverage to 20 days and physician visits per year to 12, (2) reduced drug coverage, and (3) instituted copayments of $1 per physician visit and $3 per outpatient hospital visit. However, these changes are expected to cover only about a third of the $27 million cut elected officials were seeking.

PROVIDER TAXES CATCHING ON

New provider taxes to finance Medicaid remain the hottest area of policy change in both health care financing and overall state tax policy. On other subjects -- both general tax increases and financing indigent care -- there is lots of talk and little action. On provider taxes, there is much action, but state officials are minimizing talk. Why? First, by any common sense understanding of the term, these are new *taxes* being levied by officials trying to run on the basis of not enacting new taxes. Second, the subject is understood by few policymakers and even fewer reporters.

Medicaid provider taxes, such as a gross receipts tax on hospitals, were adopted by a substantial number of states in 1991 and 1992, but by far fewer states than will eventually adopt them. Some of the states that are facing the mid-1993 deadline for eliminating provider donation financing haven't yet acted. **Illinois** was the latest state to act. It adopted over $700 million in provider taxes in July as part of the compromise FY 1993 budget. The governor told reluctant providers their alternatives were an unlikely income tax increase -- which he and a majority of legislators oppose -- or sharp cuts in Medicaid reimbursement rates. **Missouri** also recently adopted a hospital provider tax.

The reaction of provider groups to the provider tax proposals has been inconsistent both among different providers in the same state and the same providers in different states. **Reports** perceives provider support increasing for three reasons. First, decreasing time between the decision and the time existing donation and disproportionate care programs become invalid under current federal law. Second, increasing perceptions, where applicable, that state elected officials won't raise taxes, or that if they do the funds will be spent as promised on education, not health care. And third, increasing willingness by state officials to cut deals with providers involving other issues, particularly reimbursement rates.

Providers have been opposing, and are likely to continue to oppose, provider taxes when the revenues would be used for new initiatives in health care. Financing new services is less popular than paying for the increased costs of the Medicaid services already provided, with each provider group's share of the taxes roughly equal to each group's share of Medicaid spending. The governor's proposal in **Delaware**, as announced in June, is an example of a new tax associated with new spending that was being opposed by providers.

However, the new **Minnesota** HealthRight plan extends health insurance coverage to uninsured households not eligible for Medicaid. This is financed with both a cigarette tax increase and a 2% tax on gross provider revenues. The state's hospital and doctor associations objected to the provider taxes and urged higher income taxes to pay for the plan, but couldn't convince the governor or legislature. They could be back to fight another day. The hospital taxes aren't effective until 1993. The other major provider taxes don't take effect until 1994. A 1% tax on health insurance premiums and health maintenance organizations isn't slated to be in effect until 1996. Providers weren't losers from the package. It contains Medicaid rate increases such as 20% for outpatient hospital care and 25% for physicians.

In **Arkansas**, the Coalition for a Healthier Arkansas is seeking to enact a $0.25 cigarette tax increase with support of the hospital association, which likes the measure as an alternative to provider taxes.

Federal Policy Still In Doubt: Uncertainty remains over provider taxes as the federal government hasn't yet implemented the regulations to implement last year's legislation. When 14 governors visited with Bush Administration officials in June, they were told by the Health and Human Services Department deputy secretary, "The only thing more important than getting the regulations out quickly is getting them out in good shape."

One argument for adoption of a compromise {the 1991 law) as opposed to a moratorium was that the governors wanted some certainty in the law so that they could make decisions. But the proposal that was adopted was flawed in that it did not give the certainty, the guidance, needed to pin this issue (provider assessments) down and put it behind us. -- U.S. Representative Waxman, quoted in State Health Notes, (3/23).

GAMBLING AND LOTTERIES

The Spread Of Legalized Gambling: Legal gambling is now easily accessible to nearly every American. By one count, some form is already available in every state but Hawaii and Utah. In many of the states that have been the slowest to move to modern legalized gambling, charity Bingo and casino nights are widespread.

As more states have adopted lotteries, racing, and other forms of gambling, it is increasingly clear that state prohibitions are not preventing state residents from gambling. Stories of lottery pools to invest in tickets of other states, bus charters to Atlantic City casinos and neighboring-state race tracks, and massive sales in tiny stores just across the border into a lottery neighbor of a non-lottery state are common. All strengthen the case that state access to gambling jobs and state revenue, not residents' access to gambling, is being restricted by gambling prohibitions. Public opinion polls and voter approval of gambling in other states is convincing reluctant elected officials of public support.

But like a high-roller on a hot streak, most states aren't worried about the long run. The fever has taken hold, and the promise of quick payoffs is still too tempting to pass up. To the voices of caution, the gamblers' answer is "let it ride." -- Gambling Fever: Odds Are, You've Got It, Midwestern Legislative Conference Of The Council of State Governments (1992).

Changing Opposition To Gambling: Some state officials and religious groups have tried to buck the trend or at least slow the rush. There appears to have been a change in the source of opposition to new legalized gambling proposals. The importance of moral objections has shrunk considerably to a few bastions -- the Mormon church in the West and Christian fundamentalists in the South. Now the strongest opposition to extension of legalized gambling comes from beneficiaries of old legalized gambling fearful of new competition.

Some of this opposition is formidable because it brackets the sources of influence in state policymaking. On the one hand are groups clearly representing large numbers of ordinary citizens -- religious groups, volunteer fire departments, and other bastions of the community. On the other are the already legalized operators, such as race track owners, with their strengths in the behind-the-scenes atmosphere of campaign finance, as well as lobbyists who are established figures in their state capitols.

Gambling Appears Secure: It is conceivable that some event would turn back the current trends, but it is hard to imagine what it might be. So many people have vested interests in the continuation and expansion of present legalized forms of gambling that it is most unlikely that the feared corruption of legalized gambling, even if it materialized in several states at once, would cause abandonment of gambling any more than evidence of corruption in Medicaid has caused its abandonment.

Lotteries Becoming Mature: With the Texas lottery now underway and Georgia and Nebraska voters likely to approve lotteries in November, 37 states, including all the major industrial states, will be in the lottery business. Some of the Northeastern lotteries are now over 20 years old, meaning that a whole generation has come of age without any recollection of periods without lotteries. Only a few of the major lotteries are so recently established that their sales are subject to both the stimulus of start-up excitement and the lower per capita sales associated with start-up processes. Except for states which established lotteries in 1989 or later (* in the table below) per capita sales reflect long-term differences among states.

Per Capita Lottery Sales, CY 1991

Rank	State	Amount	Rank	State	Amount	Rank	State	Amount
1	Massachusetts	$267	13	Delaware	$107	23	Colorado	$64
2	South Dakota	198		**United States**	**109**	24	California	61
3	Maryland	169	14	Kentucky*	95	25	Washington	59
4	Florida	167	15	New Hampshire	87	26	Arizona	56
5	New Jersey	165	16	Wisconsin	85	27	Iowa	56
6	Connecticut	163	17	Vermont	83	28	Idaho*	50
7	Ohio	151	18	Maine	81	29	West Virginia	47
8	Illinois	140	19	Indiana*	75	30	Missouri	42
9	Virginia	133	20	Oregon	69	31	Louisiana*	38
10	Michigan	124	21	Rhode Island	66	32	Kansas	31
11	Pennsylvania	122	22	Minnesota*	65	33	Montana	31
12	New York	113						

The disparities in per capita lottery play are substantial, with the Massachusetts total more than twice the national average. Six states are at half or less of that average. Many explanations are possible for the differences. They include factors under the control of state governments such as the variety of games available, the restraints states place on advertising, the percentage of revenues available for prizes, the prize structure (mix of small and large prizes), the size of the state (and thus the size of typical jackpots), and the skill of each state's lottery administrators. Other variables relate to the state's demographics. Some population groups bet more than others. States are unequally endowed with those populations. Finally, there are competitive factors beyond state control, such as whether neighboring states have lotteries.

Lottery Sales Growth: Over the past year, state lottery sales have grown by only 0.5%. When adjusted for the number of persons in lottery states, revenues shrank by half a percent as shown in the table.

Percentage Change In Lottery Sales, CY 1990 - CY 1991

Rank	State	Percent	Rank	State	Percent	Rank	State	Percent
1	Kentucky*	81.9%	13	Delaware	1.6%	23	Michigan	-2.9%
2	South Dakota	45.2	14	Illinois	1.6	24	Missouri	-3.3
3	Oregon	29.0	15	New Hampshire	0.5	25	Pennsylvania	-5.2
4	Colorado	27.3	16	Connecticut	0.2	26	Montana	-5.3
5	Virginia	26.5	17	Vermont	0.2	27	Florida	-5.4
6	Minnesota*	16.2	18	Maine	0	28	Idaho*	-7.3
7	Washington	14.4	19	Rhode Island	0	29	Iowa	-9.1
8	Kansas	12.6		**United States**	**-0.5**	30	Indiana*	-9.9
9	West Virginia	11.6	20	Ohio	-1.3	31	California	-20.7
10	Wisconsin	11.0	21	Maryland	-1.8	32	Arizona	-29.6
11	Massachusetts	2.9	22	New York	-1.9	33	Louisiana*	N/A
12	New Jersey	2.7						

While there is great variation among states (which **Reports** cannot explain), the budget message for the large industrial states is that lottery revenues didn't exhibit significant growth, and actually declined in many. The 1991 results are the first serious demonstration that state lotteries are not a powerful revenue engine that can be counted on to grow by at least the rate of inflation in good times and bad. The recession apparently had effects on the purchase of lottery tickets similar to its effects on other consumer purchases. Even in better economic times, the large-state lotteries have been unable to maintain the rapid growth of their early years. For example, declining lottery revenues for schools in **California** have strengthened the resolve of education interests to fight for the constitutionally guaranteed share of state revenues under Proposition 98.

Earmarking Lottery Revenues: The lack of growth in lottery revenues and the instability suggested by large gains and losses among individual states is not much of an argument against having lotteries. It is a substantial argument against earmarking lottery revenues for a stream of expenditures that exhibits a steady profile of growth. The resulting problems have been particularly severe in **Pennsylvania**. Most states earmark money for education. But Pennsylvania's earmarking is for programs for the elderly, particularly subsidizing the purchase of prescription drugs. As these costs have grown in some years much faster than lottery revenues, Pennsylvania decisionmakers have been confronted with the awkward choice of scaling back spending or financing a portion from general revenues.

Other Gambling Forms Advance: The states now appear to be moving quickly into new forms of gambling such as video poker (called video lottery terminals) and casino gambling in special situations -- ships to nowhere, riverboats, and historical towns. **Colorado** and **South Dakota** both have historical towns which are currently operating casinos. **Illinois**, **Iowa**, **Louisiana**, and **Mississippi** have all approved riverboat gambling. **Missouri** voters will consider riverboats in November. Gambling on Indian reservations is providing an impetus to gambling in some states, sometimes in peculiar and unpredictable ways (see box).

Many want their states to be among the leaders in the latest gaming innovation. This year the **Louisiana** legislature authorized a casino in New Orleans. Temporary tables could be in operation as early as next spring. However, there will be litigation over whether the action conflicts with a state constitutional provision: "Gambling shall be defined by and suppressed by the legislature." Chicago business and government leaders are asking the **Illinois** legislature to adopt a multiple-casino plan for the Windy City. There are similar proposals for Cleveland, Detroit, Hartford, Milwaukee, and other large cities.

Indian Gambling, The Wild Card

The complex ground rules for gambling on reservations boil down to the concept that states cannot prohibit tribes from offering gambling opportunities that are legal anywhere in the state. The interaction of this rule with charity gambling statutes, the wording of lottery amendments in individual states, and conflicting interpretations of federal rules and state laws has created near chaos in some states.

Governors and legislatures are frequently getting crosswise on the issue, as has happened in Connecticut and Kansas. The situation in Wisconsin is so complex that it defies explanation in anything short of a book-length treatise. The speaker (D) offered the governor (R) an oblique compliment by commenting, "This is the only issue he has managed to totally screw up in his 5 1/2 years as governor." The Wisconsin Taxpayers Alliance recently suggested that as a result of the decision to put a five-question advisory referendum on the April ballot, "Come April 1993, the gambling waters might be even muddier than now."

Iowa is offering "lottery" tickets in vending machines that let the purchasers buy paper tickets and pull off ticket coverings with the same results as pulling a slot machine lever -- matching fruits and other symbols for prizes. Other pull-tab games simulate blackjack and poker. The ads say, "CASINO ACTION! As close as you can get without being there."

Video lottery machines -- video terminal versions of slot machines, computerized poker, and bingo -- have been approved in at least five states. Other states are seeking to match **South Dakota**'s success. Its revenues of $46 million in 1991 equaled the costs of its prisons and courts.

> *There is little difference between a video lottery terminal and the basic video poker or blackjack unit. Take one of the video pokers found in any Nevada or Atlantic City casino, change the glass, replace the coin hopper with a ticket printer and presto, you have a VLT. It is not much of a change but it makes all the difference to those who oppose "casino gambling" but do not feel nearly as uncomfortable with lotteries. -- Gambling & Wagering Business (12/15 1991)*

Sports betting has been approved in **Delaware** and **Oregon** in addition to **Nevada** which has allowed it for decades. The National Football League is so alarmed by the trend it is asking the Congress to outlaw the practice.

The bounds of ways to legalize gambling are tested by a tongue-in-cheek proposal in New England to take the controversial Seawolf submarine and convert it to underwater gambling, one-upping the riverboats of the Midwest. As one proponent puts it, "Far from being above the law, participants will now remain safely below it."

Gambling Economics: The state gambling proposals have produced extreme claims of economic benefits. A technical note applying conventional analytic techniques appears at the end of this issue. The different claims were recently exhibited in **Louisiana** with vast differences between opponents and proponents, and even among proponents, in predicted economic impacts of a new casino. Ironically, the site is a convention center area available because optimistic claims for it haven't been realized. Recent separate **Illinois** studies credited $1.4 billion in economic activity to horse racing and credited the proposed Chicago casinos with a $3.7 billion impact. The state and local tax impact was estimated at 5.7% of total impact in the horse racing study and 14% in the casino study.

The continuing caveat on all claims for extraordinary returns from legalized gambling is that competition among states and among forms of gambling will tend to reduce returns over time. Examples: the national movement to cut state taxes on horse and dog racing, pressures to reduce the state percentage from lotteries, and moves to end limits on riverboat gambling in **Iowa** because of **Illinois** competition.

FISCAL UPDATE

Calm Before The Storm

The months of July through November are usually quiet periods in state fiscal decisionmaking, particularly in election years. This year is no exception in most states. Legislatures aren't in session. Leading elected officials are worrying about national party conventions and the fall campaigns. Staff members are going to their annual conventions and taking vacations. Information that is the grist for the fiscal mills -- new economic forecasts, monthly revenue performance reports, indications of agency needs for supplemental appropriations -- are accumulating in many in-boxes.

In many states, as State Budget & Tax News has been suggesting in reviewing the results of the 1992 legislative sessions, the news accumulating in these in-boxes isn't good. Reasons: (1) national, and thus state, economic performance hasn't been exciting, (2) some of the assumed savings in FY 1993 budgets, particularly in Medicaid and state payroll costs, aren't being realized, and (3) many FY 1993 budgets left problems for FY 1994 by use of one-time revenues, deferral of costs, and drawing down surpluses. Staff members will find the predictable results in their in-boxes before November, but incumbent elected officials have no motivation to find problems yet.

California's Problems Won't Quit

Stalemate Continues: The big exception in the otherwise quiet summer is **California.** It has been getting national publicity for not passing a budget for the fiscal year that began in July and paying state bills with IOUs (registered warrants) to handle cash shortages. Bond ratings have already dropped and could drop again if the situation isn't resolved by actions that bond rating agencies deem to be tenable long-term fiscal policies.

California's procedures require a two-thirds vote to pass a budget, so both parties in each House must be involved in any resolution. Republican legislative leaders and the governor are holding the position simply expressed by their Senate leader, "We're in a non-negotiable mode when it comes to deficit spending ... and we're not going to encounter taxes." This posture concentrates all of the $11 billion in budget balancing believed to be needed on spending reductions. The Democrats are amenable to some spending reductions, but not as large as the Republicans seem willing to support. The gap is symbolized by the difference between a $2 billion education cut discussed by some Republicans and the $605 million cut presented to the governor and vetoed.

Emphasis On Blame Shifting: The level of partisan name-calling between the legislative leaders (D) and Governor Wilson (R) remains higher than in many states.

The governor blames the impasse on the Democrats, who blame him. They have called for future deliberations to be in open meetings so the public can decide who is being intransigent.

The governor told the press that he would rather tolerate the "chaos" from lack of resolution of the issues than "take this terrible misstep from which I think the state would never recover." That "misstep" is adopting "ruinous deficit spending as a matter of policy." He argues, "If that's allowed to happen, it will set the stage for massive, regular increases in your state taxes -- especially in your income taxes -- every year for the rest of the 1990s." The governor's communications director slammed a legislative budget proposal as a "Democratic wish list," missing only "aid to the Viet Cong."

Democrats attacked the governor from many directions. One was that he was abdicating his leadership role. Another was that he was contributing to the deadlock to improve the November election prospects of both Republicans running against incumbent Democrats and of his ballot initiative that cuts welfare and gives him new powers over the budget. Legislators of both parties do agree that continuing stalemate will make all of them look bad to the public. The speaker's comment on the governor's strategy was, "Who knows what he's thinking, if he's thinking at all."

The Fiscal Problem: While California's economic and fiscal problems are a disaster by California standards, they aren't as serious as those of some other states. In both personal income and employment changes (see Issue 12), the California economy has been performing better than the economies of **Connecticut**, **Massachusetts**, **New Hampshire**, **New York**, and **Rhode Island**. Partly because of tax increases adopted in 1991, the state's FY 1992 revenues were up about 5.2% from FY 1991. This was a respectable increase in relation to inflation and population growth.

So why is California now in so much more trouble than the economically worse-off Northeastern states? One reason is timing. Recession hit the Northeast late in the 1980s. Many fiscal adjustments, including tax hikes well above California's 1991 increases and spending austerity, have already been made. Second, expectations were higher in California. The 5.2% FY 1992 revenue increase experience in California would be news in the Northeast, but not compared with a 13.5% increase assumed for California as recently as when the governor filed his budget in January. Third, demographic trends are unfavorable. California is adding nearly 300,000 school students a year while Northeastern enrollment is stagnant. New migrants continue to pour into California, often not finding jobs but adding fiscal pressures in health and social services. Fourth, California has had a run of bad luck with fires, riots, and earthquakes.

A Preview Of Retrenchment Strategies: California officials were close to budget agreement by the June 30 deadline. Positions at that time and proposals since suggest that California's spending adjustments will look much like those of the Northeastern states:

Public schools won't get increased state aid meeting the two tests of Proposition 98: (1) matching the combination of inflation and student count increases or (2) maintaining a constant share of the state budget.

Higher education will take disproportionate hits to be covered in part by tuition increases (still leaving California tuition below most states) and in part by a reduction from current service levels. Community colleges, now protected by Proposition 98 along with public schools, will share in austerity.

Welfare grants won't grow automatically anymore, a decision already made, and may well be cut from levels well in excess of other states.

Local governments will be forced to share the state's pain, at least proportionately.

In relation to other states with underlying economic problems, California's revenue system has several features that seem likely to be reconsidered if fiscal problems continue. The first is indexing of the income tax to keep inflation from shoving taxpayers into higher tax brackets. Indexing also keeps growth in revenues from the graduated income tax from growing as rapidly as in other states. The second is the absence of provider taxes and the aggressive exploitation of Medicaid funding that has characterized the fiscal management of other states with economic problems, particularly **Massachusetts**, **New Hampshire**, and **Rhode Island**. The third is a generous public employee pension plan that is well funded, suggesting reducing costs by reduced benefits for new state and local employees (not being discussed) and simply lowering employer contributions to the present plan. The second choice is serious enough so that employee groups are banking an initiative to prevent it.

Issues Resolved In Other States

Greased by better-than-expected FY 1992 revenues, **Massachusetts** deliberations moved smoothly to a conclusion even though the process extended beyond July 1. Interim budgets were adopted without major controversy. The overall budget reflects a compromise between the Democratic legislative majorities and Governor Weld (R). The governor's proposed business tax incentives are dropped, but a phased-in estate tax reduction which he also endorsed is included.

Officials of many other states long ago finished their budgets and left the state capitols. In **Florida**, fiscal problems were patched enough so that incumbents will generally be able to return next year to resume the battle. Provider taxes were the linchpin of a similar resolution of issues in **Illinois**.

Looking Ahead To Fiscal Problems And Tax Increases

Recently a subscriber asked in which states the pressures were strongest for big fiscal decisions, including possible tax increases, to be made immediately after the November elections or early in the 1993 sessions. The answer was guesswork, of course. For what it's worth the list is: (1) the states (**California**, **Illinois**, and **Rhode Island**) with difficulties in enacting a budget by July 1, to the extent they don't resolve their problems earlier, (2) two states with gaping self-inflicted wounds, **Texas** with an unconstitutional property tax system and **Oregon** with its new property tax rollbacks, and (3) **Alabama**, **Florida**, **Louisiana**, **Michigan**, **Ohio**, **New Hampshire**, **New Jersey**, **New York**, and **Tennessee**. Other states have problems, but are less likely to have to resolve them before completing their normal budgeting process for FY 1994.

Action and inaction by the **New York** legislature before completing its session in July are indicative of issues to come. The legislature passed a status quo budget more or less on time. But it didn't act on two subjects that were the cornerstones of the governor's plan for state action to encourage economic development: (1) a bond issue that would have gone to voters in November and (2) new authority for the toll highway agency to sponsor development projects.

Empire State legislators also left several local fiscal problems unresolved. The first was the uneven and large impact of required local government cost-sharing for Medicaid. The second was coming to grips with the fiscal problems of two Long Island counties which together serve nearly as many people as most states. Nassau and Suffolk county officials have done as much budget cutting as they want to do, so they now see the alternatives as unacceptable tax increases (e.g., a 25-30% increase in property taxes) or authority from the legislature to borrow to cover operating deficits and to cover debt service by less dramatic tax increases -- a half-cent sales tax increase in Suffolk and taking a 1% cut of the amount of newly recorded mortgages in Nassau County.

HIGHER EDUCATION TAKING BIG HITS

One of the realities we have to face is that there are programs we'll never be able to go back to. ... We'll never again have the great free-tuition university system that we once knew. -- Bob White, Governor's chief of staff, California

As the **California** budget gap reached $11 billion out of a budget of $60 billion, previously unthinkable cuts become serious alternatives. One is a 15% cut in state support of universities -- more than can be handled by tuition without severe dislocations for the many students who have built education plans around tuition at or near present levels.

Even before final budget approval, the grim outlook, an 8% cut in the optimistic scenario, was forcing decisions. Four campuses announced they won't accept applications for admission this winter or next spring. About 30,000 students, including community college transfer students, will be affected by the action. The number is expected to multiply as other state institutions copy the move.

In **Ohio**, the governor made administrative cuts in July to cover expected shortfalls in the newly enacted budget. Higher education's share of the cuts was much larger than its share of the budget. Buckeye State universities and community colleges took disproportionate hits earlier, absorbing 39% of the February 1991 cuts and 29% of the December 1991 cuts. Higher education officials calculate that per-student support has dropped from $5,000 four years ago to about $4,000. Recently approved 9% tuition hikes will cover about half the most recent cut. In **Minnesota**, the oft-threatened, little-implemented step of closing a state institution is occurring. This summer the University of Minnesota at Waseca will become history.

In **Oregon**, the governor's proposal to institute a sales tax to cover losses from a voter-approved cutback of property taxes failed. The higher education community, while hoping for a reversal in the legislature, is now planning for a 20% cut in state support for the biennium that begins next year. In **New Jersey**, the funding for state colleges has been dropped to 1988 levels. The budget includes a $30 million fund earmarked for institutions that don't raise tuition by more than 4.5%. Trenton State trustees raised tuition by $105 or 4.45% but added a $500 "fee for quality."

Nationwide, the salary survey of the American Association of University Professors shows this year's faculty salaries up 2.9% at public institutions. This contrasts with about 5% at private institutions. The chairman of the AAUP committee that ran the survey concluded, "The boom days of the mid-1980s are gone."

Do these illustrations, coupled with the generally poor success of higher education in competing for FY 1993 state money, portend really rough times ahead for public universities? It is too early to tell. This may just be a repetition of a pattern by which higher education becomes a "balance wheel" of state budgeting -- absorbing disproportionate cuts in bad times but doing relatively well in good ones. The cuts being discussed in California and Ohio may just be paving the way for the tax increases being sought by the governor in Ohio and legislative leaders in California. On the other hand, the California actions may force the state into a permanent adjustment toward the policies of Michigan and the New England states. They seek to maintain quality by abandoning a low tuition strategy, but to maintain access by generous student aid. What's happening won't be clear until economic recovery is well underway.

NOTE: THE ECONOMIC EFFECTS OF GAMBLING

Many of the proponents' and opponents' assertions about the economic and budgetary effects of gambling so conflict with widely accepted conventional economic wisdom that they would be marked wrong in most public finance courses. The effects are, by conventional wisdom:

Effect On The Economy: Lotteries and other gambling are objects of consumer spending analogous to theater admissions, health care, or soap. The spending is appropriately measured net of cash rebates, whether 50% (lotteries), around 1% (soap), or 0% (health care). Because such *net consumption spending* doesn't add to consumers' resources (except indirectly in all three cases), an expansion of lottery purchases will come at the expense of other purchases. Exception: in isolated cases, as likely in housing or health care as lotteries, spending might reduce savings rates. The net consumer spending pays two basic components: (1) *costs of production* (including profits) and (2) a *government take* which is economically the same whether viewed as: (a) the state share, (b) lottery "profits," (c) a tax, (d) fees, or (e) combinations of these.

Economic Feedback From Production Costs: The immediate (first round) effect of spending that goes to cost of production is to pay some people involved (e.g., clerks selling tickets, state inspectors) and to purchase some goods and services (e.g., tickets, ticket machines, advertising time). Both result in more employment, payrolls, and purchases. So added spending on lotteries -- a new state, new games, increased sales -- unquestionably creates jobs. Added spending on soap or health care also unquestionably creates jobs. But because the consumption spending total is fixed, **more gambling doesn't add net jobs to the economy**. Neither does more soap or health care. The net effect of, for example, a new lottery on an economy will be to add jobs in gambling and subtract jobs in whatever fields the consumers would otherwise have favored. A good working assumption is that the losses and gains will be about equal.

Purchases -- such as gambling, soap, or health care -- have different effects on economies of individual states and communities. The most favorable effects are felt when purchasing power comes from outside. Casinos do well by this criterion, along with other tourism and manufacturing. Lotteries don't do well. Also, the most favorable state and local effects are felt when the costs of production are incurred inside the local economy. From this perspective, purchases of manufactured goods, like soap and cars, are worst. Health care is best. Casino gambling is good because of its high local labor content compared with outside purchases of printed tickets, video and lottery terminals, and race horses.

Economic Feedback From The Government Take: The government take pulls the consumer's money out of the private economy, costing jobs and indirect tax revenues, but spends it in the public economy, creating jobs and indirect tax revenues.

The effects of the government take are comparable across goods and services. The magnitude varies. Considering taxes on producers and sales and "profits" like those of state-liquor stores and lotteries, the take is typically 35% of selling prices for lotteries, 20-40% for cigarettes, 6-12% for liquor, 4-7% for soap, and 0-1% for health care.

From a state and local perspective, the public sector effects are comparable to the private ones. To maximize favorable local effects, it is better to get the public take from outside the local economy (e. g., tourists and out-of-state lottery players) and spend it in the local economy (e.g., on teachers and retail clerks) rather than outside (e.g., purchasing police cars or paying interest). Because government spending, whether from lottery profits or sales and other taxes, cuts the money consumers have available for other spending, **state and local government spending doesn't typically create net new jobs**.

Subsequent Economic Effects: State decisions to tax and spend more or less, to spend on schools rather than highways or the reverse, and to acquire revenues from lotteries rather than property taxes make major differences to local firms and individuals. But these differences quickly wash out in their subsequent (second round) economic effects. For example, the spending patterns of a newly hired lottery worker are not greatly different from those of a newly hired retail clerk or nurse. Because these spending patterns aren't greatly different, their impacts on state and local revenues from added taxable sales, property values, and income aren't greatly different either.

In Summary: One can speculate at length and with some justification noting, for example, that casinos generally would have favorable effects, lotteries would likely be less effective than legalizing prostitution, but more effective than legalizing drugs unless the drugs are produced in the local economy. In general, **it is a good working assumption that standard forms of gambling are associated with job gains and with indirect tax revenue gains that are about equal to the job and tax losses from however the consumer would have spent the money newly spent on gambling.**

Assessing The Fairness Of The Government Take From Gambling: Assessing the range of government takes from gambling across gambling types and comparing those takes with takes on other consumption can provide policy-relevant insights.

Against a criterion of neutrality among alternative forms of consumption, gambling takes are clearly non-neutral. The highest take as a percentage of the amount bet is in lotteries, often 35%. This contrasts with some casino games where the take of government *and* the casino operator can be as low as 2% and generally is below 10%. But the casino gambler rebets most winnings within seconds. The horse race player rebets in increments of about 20 minutes. The lottery player often rebets in weekly or daily increments. So the government take percentage can be viewed quite differently if these time differences are considered, making the government take on casino gambling appear much larger.

Viewing the government take relative to the net spending of the consumer (amount bet minus typical return in winnings) the lottery take is extremely large. A two-dollar lottery ticket purchase typically produces a net consumer outlay of a dollar. Of this 70 cents is the government take and 30 cents is the cost of administration. By this criterion, casino bets also have a large government take relative to production costs while race track betting has a much smaller percentage. Because state officials have responded to concerns that horse racing has become non-economical and tracks might close, the government take percentage on racing in many states has probably fallen below the government take on consumer purchases of products like diapers, which are subject only to standard sales taxes.

The government take from gambling, whether by tax or "profits," can be analyzed relative to income groups just as tax policy is assessed for progressivity or regressivity. On that basis, lotteries are regressive. That is, their effect is to take government revenues that are a higher proportion of household incomes of the poor than of the more affluent. This fact (which lottery advocates sometimes attempt to refute) doesn't necessarily condemn lotteries in the eyes of state decisionmakers who view lottery purchases as voluntary and accept regressivity in other taxes, such as those on cigarettes and gasoline.

TECHNICAL NOTES

Health Care: The latest book on state options is Improving Access To Health Care: What Can The States Do? (John Goddeeris and Andrew Hogan, eds., Upjohn Institute, 1992). The book omits serious consideration of proposals oriented toward greater use of free market mechanisms to regulate costs, quality, and services. For that perspective, see publications of The Heritage Foundation (214 Massachusetts Ave. NE, Washington, DC 20002) like Why The Maryland Consumer Choice Health Plan Could Be A Model For Health Care Reform (June 1992) and Medicaid: Intergovernmental Trends And Options from The Advisory Commission on Intergovernmental Relations (800 K St., NW, Washington, DC 20575).

Federal officials are having trouble writing regulations on Medicaid matching definitions for understandable reasons. White House staff members have been intervening in individual state reimbursement cases, like New Jersey's, and don't want to get the Bush Administration in a posture of cutting health care for the poor just before elections. Federal OMB officials want to prevent 30% annual cost increases. The White House may want to extend its moratorium on new regulations. Adding to the federal problem: state officials are showing considerable ingenuity in defining taxes. As the CCH State Tax Guide (3/9) described the new West Virginia "Medicaid enhancement tax," the base is the portion of Medicaid reimbursements paid from state money and the tax rate is 100%.

Comparisons of per capita health care costs among states and statistical explanations for the differences were recently reported by the General Accounting Office (Washington, DC 20548) in Health Care Spending: Nonpolicy Factors Account For Most State Differences. The report contains numbers for 50 states -- Massachusetts is tops (1990) at $3,031 per capita, well above the U.S. average ($2,425), and even more above least expensive South Carolina ($1,689). Problems with the numbers abound. For example, the statistical base is 1982 data and costs of Vermont residents receiving care in Massachusetts hospitals are probably in the Massachusetts numbers, not Vermont's. Regression analysis based on the numbers tends to be either obvious (states with higher per capita incomes have higher per capita health care spending) or circular (the costs of health care rise when the ratio of physicians to people rises OR when health care spending is higher the physician-patient ratio rises).

Comparisons of Medicaid costs among states have a much stronger basis. Unpublished information on Medicaid cost variations previously discussed in **Reports** is now available in published form (Jane Little, "Lessons From Variations In State Medicaid Expenditures, "New England Economic Review, Jan./Feb.). The Employee Benefits Research Institute (2121 K St. NW, Washington, DC 20037) has a new 60-page summary of health care reform issues, Health Care Reform: Tradeoffs And Implications. The spring issue of Intergovernmental Perspective (Advisory Commission on Intergovernmental Relations, Washington, DC 20575) is devoted to intergovernmental health care issues, primarily Medicaid.

The conclusion that not much is happening in the states in major health care reform plans depends on **Reports**' consistent skepticism about state enactments involving no current spending or revenue loss but which promise benefits with heavy budget implications in future years. **Reports** discounts heavily scheduled tax cuts, the "temporary" in temporary taxes, scheduled future increases in state school aid, promised future health plans, and similar enactments. Without this skepticism, a case can be made that there is considerable activity in state health care reform. If proposals of commissions and governors are also counted, the case is even better. See, for example, the National Governors' Association press release (6/15) on health reform initiatives and the Governors' Bulletin (7/6), both touting actions in **Delaware**, **Florida**, **Hawaii**, **Minnesota**, **Montana**, **Oklahoma**, **South Dakota**, and **Vermont**.

Gambling: The tables on lotteries and the quotations, unless otherwise cited, are from Gambling & Wagering Business (4/15). A recent book, The Economic Consequences of State Lotteries (Mary Borg and others, Praeger, 1991) is clearly anti-lottery, but contains comprehensive citations to other economic assessments.

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